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EUROPEAN SUPERVISORY AUTHORITIES' CONSULTATION

JOINT GUIDELINES ASSESSMENT OF THE SUITABILITY OF MEMBERS OF THE MANAGEMENT BODY AND KEY FUNCTION HOLDERS UNDER DIRECTIVE 2013/36/EU AND DIRECTIVE 214/65/EU

On 28 October 2016, the European Banking Authority ("**EBA**") and the European Securities and Markets Authorities ("**ESMA**") initiated a consultation on joint guidelines on the assessment of the suitability of members of the management body and key function holders under Directive 2013/36/EU(the "**CRD IV**") and Directive 2014/65/EU ("**MiFID II**")[1] (the "**Draft Guidelines**").

1 In their consultation paper, the EBA and the ESMA propose Draft Guidelines to establish criteria for the assessment of the suitability of the members of the management body of institutions[2] (the "**Institutions**") and certain other key function holders[3], in order to further improve and harmonize this suitability assessment within the EU financial sector and ensure sound governance arrangements.

To this effect, a number of recommendations are proposed on the different notions of suitability as required by Art. 91(12) of the CRD IV and Art. 9(1) of MiFID II and on the assessment of suitability by institutions and competent authorities.

It is intended that the EBA's current guidelines on the assessment of the suitability of members of the management body and key function holders[4] (the "**Current EBA Guidelines**") will be repealed following the finalisation of the Draft Guidelines.

2 Given the different impact that the Draft Guidelines will have on individual member states (depending on their current regimes), we are submitting our comments to the Draft Guidelines on a jurisdiction by jurisdiction basis[5]. Therefore the comments below in relation to an individual jurisdiction are only applicable to that jurisdiction.

Nonetheless, we have grouped together comments which are applicable to more than one jurisdiction.

[1] EBA/ESMA, Consultation Paper – Joint ESMA and EBA Guidelines on the assessment of the suitability of members of the management body and key function holders under Directive 2013/36/EU and Directive 2014/65/EU (EBA/CP/2016/17), 28 October 2016; Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and investment firms and Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments.

[2] Credit institutions, financial holding companies, mixed financial holding companies and investment firms as provided under paragraph 13 of the Draft Guidelines.

[3] Heads of internal control functions and the CFO, where they are not part of the management body, of credit institutions and certain investment firms and, where identified on a risk-based approach by those institutions, other key function holders, pursuant to paragraph 6 of the Draft Guidelines.

[4] EBA, Guidelines on the assessment of the suitability of members of the management body and key function holders (EBA/GL/2012/06), 22 November 2012.

[5] *Bonelli Erede*: Italian law; *Bredin Prat*: French law; *De Brauw Blackstone Westbroek*: Dutch law; *Hengeler Mueller*: German law; *Slaughter and May*: English law; and *Uría Menéndez:* Spanish and Portuguese law.

3 General remarks

Germany: In our view, the Draft Guidelines are much too granular, prescriptive and extensive. An excess of detailed criteria creates more rather than less legal uncertainty both for institutions and competent authorities when assessing the suitability of members of the management body. In addition, this may lead to arbitrariness when making suitability decisions by competent authorities with the risk that the nature, scale and complexity of the institutions will not be taken in due consideration and the principle of proportionality will be overlooked.

This holds, in particular, true for the amount of information to be taken into account by institutions and competent authorities under Annexes I to III of the Draft Guidelines.

Therefore, we recommend that more flexibility be left to institutions when implementing the principles of the CRD IV and MiFID II. Assessment and notification processes should be simplified and should strictly adhere to the principle of proportionality.

Germany, Spain and Portugal: EBA and ESMA should also coordinate their work with the draft guide to fit and proper assessments (the "Draft ECB Guide") as published by the European Central Bank (the "ECB") on 14 November 2016.

This relates in particular to the situations where the Draft Guidelines and the Draft ECB Guide require Institutions to re-assess the individual and collective suitability of the members of the management body.

Pursuant to paragraphs 16 and 25 of the Draft Guidelines, the individual suitability of the members of the management body and the collective suitability of the management body should be re-assessed when re-appointing members of the management body, *inter alia*, if the requirements of the position have changed or the member is appointed for a different position within the management body.

Under the Draft ECB Guide, a fit-and-proper assessment can be triggered by a change in the management body, owing to a new appointment, a change of role or a renewal (see Chapter 7 of the Draft ECB Guide). According to the ECB, a change of role occurs if it is proposed that a non-executive member is appointed as executive director or vice versa; or a member is appointed as chairperson, as chairperson of one of the specialised committees in the management body or as CEO. In addition, the ECB clearly sets out that a fit-and-proper assessment will only be made for changes in the management body, including renewals, if required and as defined by national law (see Chapter 7.1 of the Draft ECB Guide).

In this respect, the misalignment between the Draft Guidelines and the Draft ECB Guide raises doubt as to the relevant events which may trigger a suitability assessment of a re-appointed member of a management body. This should be clarified in the finalised guidelines.

In particular, we kindly suggest to confirm that the renewal of the time-limited appointment of a management body's member does not require, per se, an *ex-ante* suitability assessment. Furthermore, the cases in which a member is considered to be appointed for a different position within the management body should be clarified. With reference to the second aspect, we feel that a relevant change of role occurs only in the case in which a non-executive director is appointed as an executive director.

UK: The UK regulatory regime has had, for many years now, both under the FCA and PRA, and before that under the FSA, a well-established procedure to assess the fitness and propriety of relevant individuals in all regulated institutions. These assessments operate on an *ex-ante* basis. In general, in our view, this procedure has worked effectively, and successfully struck the right balance between higher level requirements and more specific guidance. This has allowed assessments to be carried out effectively and provided flexibility in individual situations, depending on the nature, size and complexity of the institution, the role for which the assessment is being undertaken, and the proposed candidate selected to perform that role.

In contrast to the balance struck under the UK regime, we consider that the level of detail and granularity contained in the Draft Guidelines could hamper the effective operation of, and compliance with, the Guidelines.[6] While we appreciate that this level of detail has, potentially, been included to clarify the requirements, its inclusion has the potential to result in an overly rigid process and one that does not allow flexibility in individual situations.

We also suggest that, insofar as is relevant, the Draft Guidelines are consistent with the ECB's proposed 'Draft guide to fit and proper assessments', published on 14 November 2016 and currently the subject of consultation ('the ECB Draft Guide'). This consistency will assist compliance by institutions which are subject to both sets of guidance, and should also assist the ECB in its compliance with the Draft Guidelines (as referred to in paragraph 1.3 of the ECB Draft Guide). By way of example, the suitability assessment triggers for individual members of the management body, set out in paragraph 16 of the Draft Guidelines, should be consistent with the assessment triggers set out in the ECB Draft Guide, Chapter 7, first unnumbered paragraph.

Italy: We welcome the contents of the Draft Guidelines, which aim to overcome some of the shortcomings emerging from the inspections of some Italian banks recently carried out by the ECB and by the Bank of Italy.

On the other hand, we believe that the provisions set forth in the Draft Guidelines are extremely detailed. We are aware that, to some extent, detailed provisions are coessential to any guidelines, but our concern is that the obligations set out in the Consultation require time-consuming activities in order to implement the relevant provisions of the guidelines, as well as consistent resources. Therefore, the compliance with the final guidelines could be quite expensive for the Institutions involved, thus jeopardising the enforcement of the guidelines and, consequently, the overall harmonisation of the fit and proper assessment of the members of the management body.

In this respect we would like to point out that in the consultation on corporate governance rules that led to the amendment to Circular no. 285 of the Bank of Italy, the Italian authority rejected the requests for more detailed rules as submitted by the participants in such consultation. The Bank of Italy explained that such refusal intended to grant banks a degree of autonomy in their decision-making process, for which they are solely responsible.

Overall, the suitability assessment of the members of the management body - as corporate governance rules in general - is a sensitive matter as it greatly affects the internal organisation of the Institutions. Procedures, policies and day-by-day operations are deeply affected by corporate governance rules. Therefore, we believe that a degree of autonomy and flexibility in the decision-making process should be granted to the relevant institution by the final guidelines.

* * *

Q1: Are there any conflicts between the responsibilities assigned by national company law to a specific function of the management body and the responsibilities assigned by the Guidelines to either the management or supervisory function?

Spain and Portugal: References to the independence of mind and challenging capacity of directors should be adapted in relation to executive directors in unitary board structures (as opposed to two-tier board structures with separate management and supervisory boards). In these structures it is natural that those executive directors "support" decisions of the management of the institution, since such decisions would have been promoted and led by them. However, this should not be regarded as a

[6] We observe that the Current EBA Guidelines is approximately 20 pages before annexes, in contrast to the Draft Guidelines, which are almost 60 pages before annexes.

lack of independence of mind and such independence should be reinterpreted in these cases as the capacity to be critical with decisions made and to extract lessons from the outcomes of past decisions.

Q2: Are the subject matter, scope and definitions sufficiently clear?

Germany and Italy: With reference to the date of application, Paragraph no. 14 of the Draft Guidelines clarifies that "These guidelines apply from 6 months after the publication of the final Guideline in all languages of the European Union".

The guidelines shall then be implemented by the competent national Authority. In implementing the final guidelines the competent authority may set a period of time to allow the relevant Institutions to comply with the guidelines.

The adequacy of such period of time to comply with the final guidelines should be assessed by considering, among other things, the specific needs of all the different Institutions falling into the scope of the Consultation.

France, Spain and Portugal: About the date of application, it should be clarified that the Guidelines shall only apply to appointment applications that are filed after their entry into force.

Germany: Paragraph 7 of the Draft Guidelines regarding the guidelines' addressees is not sufficiently clear. It does not name financial holding companies within the meaning of Art. 4(1) point (20) of Regulation (EU) No. 575/2013 (the "CRR") although they seem to be covered by the Draft Guidelines.

Spain and Portugal:

- Scope: In paragraph 10, reference is made to the guidelines applying on individual, sub-consolidated and consolidated basis. Under the proportionality principle, directors of non-relevant subsidiaries which are not regulated entities should not be subject to a fit and proper analysis. Consequently, it would be advisable to clarify that the personnel at subsidiaries (including directors) is subject to these requirements if they can be considered as "key function holders" at group level. The definition of "key function holders" is consistent with this approach, but it should be clarified that directors of non-regulated subsidiaries have to pass this test as well, rather than for the mere fact of being a member of the management body be automatically subject to the fit and proper analysis.
- Definitions: In the definition of "Significant institutions" it could be clarified that it is not referring to the definition of institutions subject to the direct supervision of the European Central Bank pursuant to the SSM Regulation.

Q3: Is the scope of assessments of key function holders by CRD-institutions appropriate and sufficiently clear?

Germany and Italy: Paragraph 31 of the Draft Guidelines requires CRD-institutions[7] to assess the reputation, honesty, integrity, knowledge, skills and experience of their key functions holders using the same criteria applied for the assessment of the suitability of the members of the management body.

With regard to this requirement, we consider that EBA goes well beyond its mandate as there is no legal basis in Art. 91 CRD IV to apply the same regulatory provisions and requirements to both the members of the management body and the key function holders of a CRD-institution. Furthermore, it goes too far to suggest that these requirements should be inherent in the notion of 'robust governance arrangements' as set out in Art. 74 or 88 CRD IV.

The above is also expressly confirmed in the draft cost-benefit analysis/impact assessment attached to the Draft Guidelines in which it is stated that limiting the suitability assessment to the members of the management body "*would restrict the assessment to what is explicitly required under EU legislation*" (see draft cost-benefit analysis/impact assessment, page 72).

[7] As defined in paragraph 13 of the Draft Guidelines.

Given this framework, it is our view that the application of the same criteria to assess the suitability of the key function holders and the members of the management body does not take in due regard the differences existing between their powers and responsibilities and ignores the principle of proportionality. In particular, Institutions already assess the experience and reputation of their key function holders as required by the Current EBA Guidelines whereas the Current EBA Guidelines leave it to the Institutions to define suitability criteria for their key function holders. Therefore, the Draft Guidelines would result in additional costs related to changing the assessment process and the documentation of the assessment results.

In light of the above, we kindly suggest to amend the Draft Guidelines in order to enable CRD-institutions to define their own criteria for the assessment of the suitability of key functions holders. There is no legal basis for the extension of the scope of the assessment to key function holders.

Q4: Do you agree with this approach to the proportionality principle and consider that it will help in the practical implementation of the guidelines? Which aspects are not practical and the reasons why? Institutions are asked to provide quantitative and qualitative information about the size, internal organisation and the nature, scale and complexity of the activities of their institution to support their answers.

Spain and Portugal: In general terms, we agree with the Draft Guidelines' approach to the proportionality principle considering that larger Institutions will need to put in place more burdensome governance arrangements, which may prove inefficient (from a cost and operational perspectives) in smaller Institutions.

France: As for Spain and Portugal, we agree in general terms with the Draft Guidelines' approach to the proportionality principle for France. However, we kindly suggest clarifying, from a practical standpoint, how the proportionality principle applies in relation to the honesty / integrity requirement, in particular as regards ongoing investigations or prosecutions, and how it relates to the presumption of innocence (please see our comments under Q7).

Italy: To the extent permitted by the relevant regulatory framework the final version of the guidelines should consider the differences between the various Italian institutions falling within the scope of the guidelines.

In fact, with reference to the Italian banking sector, it should be noted that there are material differences between the existing Institutions in terms of size, type of business, link to a geographical area and applicable corporate law (i.e. *banche popolari* and *banche di credito cooperativo*).

This is the reason why we suggest that the proportionality principle and a case-by-case evaluation approach be considered when enforcing the final guidelines concerning the assessment of the suitability of members of the management body and key function holders, also bearing in mind the specific features of the Italian banking sector.

Q5: Do you consider that a more proportionate application of the guidelines regarding any aspect of the guidelines could be introduced? When providing your answer please specify which aspects and the reasons why. In this respect, institutions are asked to provide quantitative and qualitative information about the size, internal organisation and the nature, scale and complexity of the activities of their institution to support their answers.

Spain and Portugal: It would be helpful that the Draft Guidelines also provide some guidance regarding the application of the proportionality principle in the group context, given that Institutions are required to apply fit and proper requirements at individual, consolidated and sub-consolidated level. For example, the principle of proportionality could provide some room in relation to the appointment of independent directors at small and non-complex institutions within a banking / investment firms group, especially in those jurisdictions where regulations transposing Directive 2013/36/EU have not included the possibility that those institutions do not establish appointments, remuneration and risks committees (which shall be at least

composed by 1/3 of independent directors)[8]. In relation to this matter, it should be noted that in some jurisdictions (e.g. Spain), if definitions of independent directors set forth in securities market regulations[9] were applied to all institutions –even if they are not listed companies–, independent directors at the parent institution may not be considered at the same time as independent directors of other institutions within the same group[10] and therefore the establishment of the aforementioned committees and the general recommendation of having a sufficient number of independent directors[11] can be too burdensome for groups with a large number of subsidiaries (even if those subsidiary institutions are not "significant" in the sense described in the Draft Guidelines). It is therefore suggested that the guidelines clarify that, under certain circumstances, and in line with the proportionality principle, a director may be considered as independent in different institutions within the same group[12].

France: We kindly suggest that the Draft Guidelines take into account two additional factors for applying the proportionality principle:

- On the one hand, in order for the public or semi-public nature of a supervised institution to be taken into account for assessing the appropriate implementation of the requirements set out in the Draft Guidelines. Article 2.5 of the CRD IV expressly provides that certain types of institutions do not fall within its scope. For these institutions, which include several institutions of public or semi public nature, applicable suitability requirements (including with respect to the suitability of members of their management body) are set by local law and can be adapted by each member state to the particular nature of the institution. However, certain semi-public institutions have not been included in this list and are thus subject to all rules applicable to private companies. In certain cases, these rules do not match the particular nature of the semi-public entities. For example, requirements relating to the lack of conflict of interests, targeting in particular political influence or political relationships, cannot be applied to entities whose management body members are appointed by a government act. It is therefore suggested to clarify that the public nature of an institution is a criteria to take into account when applying the principle of proportionality.
- On the other hand, in order for the mutual nature of an institution to be taken into account for assessing the appropriate implementation of the requirements set out in the Draft Guidelines. Some of France's largest banking groups have adopted the form of mutual banking groups (such as Credit Agricole, Credit Mutuel or BPCE). However, these large banking groups do not clearly benefit from certain intragroup exemptions provided in the Draft Guidelines, such as:
    - Taking into account possible synergies between positions held within the same group when assessing the time commitment of a member (paragraph 39);
    - Counting all directorships held (i) within the same group, (ii) within undertakings in which the institution holds a qualifying holding, but that are not subsidiaries included within the same group, (iii) in qualifying holdings held by multiple institutions of a same group or (iv) within the same institutional protection schema, as a single directorship (paragraphs 48 - 51).

[8] In Spain, all institutions, regardless of their size and complexity must have a risk committee (or a joint risk and audit committee) (articles 31, 36 and 38 of Law 10/2014). Wholly-owned subsidiaries of an institution may be exempted from the obligation to have appointments and remunerations committees if they are exempted from capital requirements at individual level and they rely on the relevant committees at the dominating entity (article 36.5 of Royal Decree 84/2015).

[9] Applicable definitions of independent director (for listed companies): (i) Spain: article 529 duodecies of the Companies Act (*Ley de Sociedades de Capital*); (ii) Portugal: "Governance Code of Listed Companies - Recommendations" (CMVM 2013), recommendation II.1.7.

[10] In Spain, article 529 duodecies of the Companies Act (*Ley de Sociedades de Capital*) provides that any director of a company "X" who is also a senior manager or a director of any other company within the group of the dominating entity to which "X" belongs shall be considered a proprietary director (*consejero dominical*) of "X" and thus not an independent director thereof.

[11] See page 11, paragraph 36, of EBA/CP/2016/17.

[12] If this response to Q5 leads to changes in the EBA and ESMA guidelines, section 5.3, sub-section on Disclosure, mitigation, management and prevention of conflicts of interest, of the ECB "Draft guide to fit and proper assessments" (November 2016) should also be amended.

In fact, the definition of the term group provided for in the Draft Guidelines refers to the definition of articles 2(9) and 2(10) of directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 defining a group as "a parent undertaking and all its subsidiary undertakings", a parent undertaking being defined as "undertaking which controls one or more subsidiary undertakings". It is therefore unclear whether this definition covers mutual banking groups where there is no parent undertaking which, from a share capital point of view, controls all entities. In addition, these mutual banking groups have in practice not been qualified as institutional protection schemes.

Q6: Are the guidelines with respect to the calculation of the number of directorships appropriate and sufficiently clear?

Italy, Spain and Portugal: The Draft Guidelines clearly point out that directorships in Institutions that do not pursue commercial objectives shall not be taken into account in the calculation of the directorships.

The ECB Draft Guidelines also clarify that the criteria for the calculation of the directorships shall be applied whether or not the directorships are remunerated. We suggest that this clarification be included in the guidelines that are the subject matter of the Consultation.

France, Italy, Spain and Portugal: Firstly, in relation to the general requirement of sufficient time commitment (in which the limitations on the number of directorships are framed), the following amendments could be introduced:

- Deletion of paragraph 38 is suggested, since references to an appropriate "buffer" of time to face periods of increased activity seem vague and do not favour legal certainty. In addition, the adequacy of such "buffer" may not be easily assessed where no extraordinary operations are planned or expected. Besides, such higher level of commitment required in those circumstances is implicit in the general responsibility and loyalty duties of any company director and Institutions would expect their directors to make their best efforts under those circumstances; and
- In relation to letters b (travel time) and c (number of meetings) of paragraph 39 – which sets out the criteria to assess the time commitment –, it should be taken into account whether the institution enables remote access (e.g. by conference call or videoconference) to meetings of the board of directors or board committees. On a separate note, deletion of letter h of such paragraph is suggested (or, at least, deletion of the reference to induction), since the necessary induction and training will only be particularly time consuming for a limited period of time after his or her appointment and should not prevent assessing that a director will devote sufficient time to fulfil his or her duties.

Germany, Spain and Portugal: We support the approach of the Draft Guidelines to define the counting of directorships for significant Institutions within a 'group' based on the accounting scope of consolidation.

Pursuant to paragraph 13 of the Draft Guidelines, the term 'group' means a parent undertaking and all its subsidiaries, as defined in Art. 2(9) and (10) of Directive 2013/34/EU. We understand that this definition does not only relate to parent undertakings and subsidiaries that are subject to consolidated supervision in the European Union or the European Economic Area, but also encompasses other entities provided that those entities qualify as parent undertakings or subsidiaries within the meaning of Art. 2(9) and (10) of Directive 2013/34/EU.

In addition, it might be sensible to further include in the relevant definition of 'group' groups of undertakings that are subject to consolidated supervision by a third-country supervisory authority which is equivalent to consolidated supervision carried out in the European Union on the basis of the CRD IV and Part One, Title II, Chapter 2 of the CRR. Such approach could refer to Art. 127 CRD IV and would be fully in line with the Draft Guidelines and the rationale of EBA's approach which acknowledges that, within the scope of consolidation, synergy effects exist between different directorships held by one person. Based on such an amendment, a European credit institution which is, for example, a subsidiary of a credit institution or bank holding company established in the U.S.A. and subject to equivalent consolidated supervision by a U.S. regulator could then also

benefit from the group exemption regarding the calculation of directorships. This may help to create a level playing field between those Institutions in the European Union that are subject to consolidated supervision under the CRD IV and the CRR and those Institutions in the European Union that are subject to consolidated supervision under equivalent third-country rules.

Spain and Portugal: Furthermore, it might be sensible to also include in the relevant definition of 'group' other participated entities that are institutions or financial institutions and are subject to consolidation for prudential purposes, in line with the EBA position reflected in the answer to Q&A 2014_1595[13].

Q7: Are the guidelines within Title II regarding the notions of suitability appropriate and sufficiently clear?

France: We suggest that Section 9 clarifies how the principle of presumption of innocence is to be reconciled with ongoing prosecutions, investigations or enforcement actions being taken into account to assess a person's reputation, honesty and integrity.

Pursuant to paragraph 70 of the Draft Guidelines, factors "*at least* [to] *be considered in the assessment of reputation, honesty and integrity*" include (i) ongoing prosecutions of criminal offences, the Draft Guidelines referring in particular to a list of white collar crimes and (ii) other relevant current enforcement actions by regulatory or professional bodies for non-compliance with certain provisions, "*without prejudice to the presumption of innocence*"; according to paragraph 71, certain on-going investigations should also be taken into account "*without prejudice to fundamental human rights*"; paragraph 72(d) states that civil lawsuits and administrative or criminal proceedings shall also be taken into account in so far they can have a significant impact on the financial soundness of the member or in certain entities related to the member, "*without prejudice to the presumption of innocence*".

The presumption of innocence is provided for under article 11 of the Universal Declaration of Human Rights, article 14-2 of the International Covenant on Civil and Political Rights, article 48 of the Charter of Fundamental Rights of the European Union and article 6 of the European Convention of Human Rights. This principle is thus superior to the Draft Guidelines in the hierarchy of norms.

It is unclear how in practice the requirements should be applied without violating the presumption of innocence, *inter alia* in case of persons that are subject to a current proceeding but that have not been sentenced.

In particular, it should be clarified whether, as a consequence of these requirements, in accordance with paragraph 153:

- A supervised entity would, before appointing a person that is subject to an ongoing prosecution, investigation or enforcement action, have to wait for the end of this procedure; whether this means, in case of a prosecution, that such person cannot be appointed as a member of a management body until the exhaustion of all remedies;
- A member of a management body that has already been appointed may have to be dismissed from its functions due to ongoing prosecutions, investigations or enforcement actions.

Also, the requirement of paragraph 72(d) does not clearly state whether it relates to past proceedings solely, or also to current proceedings.

Italy: Reputation, honesty and integrity: the Draft Guidelines suggest that when assessing the reputation, honesty and integrity of the members of the management body the relevant institution should consider "*any other evidence that suggests that the person acts in a manner that is not in line with high standards of conduct*". Even if we view favourably the fact that a degree of

[13] http://www.eba.europa.eu/single-rule-book-qa/-/qna/view/publicId/2014_1595.
A change of the position reflected in the answer to Q&A 2014_1595 would alter, for example, the calculation of the number of directorships if a director of an institution "X" is also a director of an institution "Y" that is not controlled by "X" but that it is included in the prudential consolidation perimeter pursuant to article 18 of Regulation (EU) Nº 575/2013.

autonomy in the assessment process should be left to the Institutions, we suggest that the meaning of "any other evidence (…)" be clarified. This provision would otherwise sound vague and might cause different interpretations of such situation, which might lead to a lower degree of harmonisation in the implementation of the relevant regulation as specified in the Draft Guidelines.

Spain and Portugal: Section 10 of the Draft Guidelines should clarify that the list of potential conflicts of interests (paragraph 77) does not prevent the appointment of proprietary directors, whom, by definition, have relationships with owners of qualifying holdings. In this regard, it should be borne in mind that corporate governance recommendations for listed companies generally accept or even foster the appointment of directors which represent significant shareholders[14] and it seems reasonable that those appointees are persons whom the relevant shareholders trust (either for personal or professional reasons)[15].

Q8: Are the guidelines within Title III regarding the Human and financial resources for training of members of the management body appropriate and sufficiently clear?

Italy: We believe that the proposed Draft Guidelines concerning training and induction are extremely detailed and might not allow the relevant institution to consider the specific features of the Institutions and the contingent needs of the members of the management body. Please see also the "General Remarks" above.

Q9: Are the guidelines within Title IV regarding diversity appropriate and sufficiently clear?

France, Germany, Italy, Spain and Portugal: Taking into account the "geographical provenance" of the member of the management body as part of the suitability assessment is, in our opinion, appropriate for Institutions of considerable size having a business model that involves national and international markets (i.e. the members of the management body should be of different geographical provenance in order to increase diversity).

By way of example, members of the management bodies coming from the same geographical area are more likely to establish a long-term relationship with the institution (as employees and then directors) and, therefore, may acquire too much power within the corporate governance structure.

However, "geographical provenance" may not be so relevant in the case of local banks, in view of their small-medium size and of the link with a geographic area.

Q10: Are the guidelines within Title V regarding the suitability policy and governance arrangements appropriate and sufficiently clear?

Germany: Paragraph 123 of the Draft Guidelines requires CRD-institutions to include a sufficient number of fully independent members in the management body in its supervisory function. Paragraph 124 sets out a list of situations where a member of a CRD-institution's management body in its supervisory function should not be considered independent.

[14] The Spanish "Good Governance Code of Listed Companies" (CNMV, February 2015) states in recommendations 15 and 16 that "*proprietary and independent directors should constitute an ample majority on the board of directors*" and that "*the percentage of proprietary directors out of all non-executive directors should be no greater than the proportion between the ownership stake of the shareholders they represent and the remainder of the company's capital. This criterion can be relaxed: a) In large cap companies where few or no equity stakes attain the legal threshold for significant shareholdings. b) In companies with a plurality of shareholders represented on the board but not otherwise related.*"
The Portuguese "*Governance Code of Listed Companies - Recommendations*" (CMVM 2013) establishes that the board of directors shall include a number of non-executive members (II.1.6), an adequate number of which should be independent, depending on the governance model adopted and the shareholder structure (II.1.7). Consequently, those recommendations recognise the possibility to appoint proprietary directors or other non-independent non-executive directors.

[15] If this response to Q7 leads to changes in the EBA and ESMA guidelines, table 1 in section 5.3 of the ECB "Draft guide to fit and proper assessments" (November 2016) should also be amended.

However, EBA's mandate under Art. 91(12) CRD IV does not cover any guidelines on the notion of 'independent members' of the management body as the presence of independent members in the management body or a part thereof is not a requirement under the CRD IV. This is also confirmed by EBA itself as it expressly states that setting out guidelines on independent members of the management body "*is not explicitly covered under the mandate mentioned in Article 91(12) of Directive 2013/36/EU*" (see draft cost-benefit analysis/impact assessment, page 76).

The requirements proposed by EBA regarding a sufficient number of fully independent members of the management body in its supervisory function also goes well beyond the concept of 'independence' recently introduced by Art. 39 of Directive 2006/43/EC as amended by Directive 2014/56/EU. Pursuant to Art. 39(1) of Directive 2006/43/EC, Member States shall ensure that generally each credit institution is required to have an audit committee the majority of the members and the chairperson of which shall be independent of the respective institution. However, where all members of the audit committee are members of the administrative or supervisory body, *i.e.*, where the audit committee is a (sub-)committee of the management body in its supervisory function of the respective credit institution, Art. 39(5) of Directive 2006/43/EC allows Member States to exempt such audit committee from the independence requirements. It is therefore the sole task and power of the (national) legislators, and not of EBA, to impose stricter independence requirements for the management bodies of credit institutions than those set out in Directive 2006/43/EC.

In addition, we are of the view that the current paragraph 124 of the Draft Guidelines on the notion of 'independence' raises doubts as to whether employee representatives may be regarded as independent members of the management body in its supervisory function. Pursuant to Art. 91(13) CRD IV, the requirements set out in Art. 91 CRD IV shall be without prejudice to provisions on the representation of employees in the management body as provided for by national law. Furthermore, Commission Recommendation of 15 February 2005 on the role of non-executive or supervisory directors of listed companies and on the committees of the (supervisory) board (2005/162/EC) expressly clarifies that a non-executive director who does not belong to senior management and has been elected to the supervisory board in the context of a system of workers' representation recognised by law could be considered as independent (see point 1(b) of Annex II to the Commission Recommendation). This is currently not yet reflected in the Draft Guidelines.

In light of the above, we kindly suggest to delete the requirement to include a sufficient number of fully independent members in the management body in its supervisory function as such requirement can legally only be set out by competent legislators of the European Union or its Member States. In the event the requirement were not to be deleted, it should be clarified and confirmed in the finalised guidelines that employees of a credit institution who do not belong to senior management and have been elected to the management body in its supervisory function in the context of a system of workers' or employee representation could be considered independent.

Italy: In our opinion the Draft Guidelines do not consider a proportionate approach to the requirements of the policy regarding the assessment of the suitability of members of the management body.

For example, in addition to the requirements concerning the tasks of the nomination committee, the Draft Guidelines also proposed the active involvement of the human resources function. It should be noted that in small- or medium-sized Institutions this may result in an overlapping of the duties attributed to this function and to the nomination committee.

Therefore, in our opinion the allocation of tasks in the suitability policy should be defined by the management body of the entity by taking into consideration the specific features of the institution.

Spain and Portugal: Firstly, the provisions in paragraph 119 should not prevent directors who are not members of the appointments committee from contributing to the selection of candidates for vacant management positions by submitting to the committee potential candidates for its assessment[16].

Secondly, section 18 of the Draft Guidelines provides a definition of independent director that may conflict with legal definitions in each Member State. Where statutory definitions apply, those should prevail over the guidelines if they are more restrictive but it should be clarified what is the EBA position if the guidelines are more restrictive.

In addition, in certain jurisdictions (e.g. Spain, Portugal) those definitions are included in regulations which apply to listed companies and therefore it may be interpreted that non-listed institutions are not subject to those definitions. However, due to the absence of a specific definition of independent directors applicable to all institutions, supervisors have in practice been applying those definitions provided for listed companies. Consequently, if the final guidelines were to include specific independence criteria, it would be advisable that they clarify that non-listed institutions are not required to apply the definitions for listed companies.

Q11: Are the guidelines within Title VI regarding the assessment of suitability by institutions appropriate and sufficiently clear?

Spain and Portugal: We consider that the last sentence in paragraph 127 should be clarified: on the one hand, it should be described how shareholders must be informed about the assessment made by the Institutions (e.g. would a material fact announcement or a notice in the corporate website be enough?); and, on the other hand, it should be confirmed that if the institution came to the conclusion that the candidate appointed by shareholders is not suitable, the board of directors may directly appoint a different member by co-option (where such procedure is available at the relevant jurisdiction[17]) without the need to call a new general shareholders meeting where shareholders nominate new candidates. Since directors appointed by co-option shall be ratified by shareholders at the first general shareholders' meeting held after the appointment, this seems to be a reasonable and cost-efficient approach.

Paragraph 130 could be supplemented with a provision stating that the same result can be achieved by including in the corresponding corporate resolution a condition precedent preventing the appointment becoming effective until the competent authority has verified the suitability of the appointee (see also responses to Q12 below).

Germany: Title VI of the Draft Guidelines provide for various communication and notification obligations of Institutions *vis-à-vis* competent authorities which are neither part of the Current EBA Guidelines nor are they foreseen in CRD IV or MiFID. It is therefore not the mandate of EBA, but, unless the respective level 1 text is not amended accordingly, the power and task of the competent national legislators to impose additional notification obligations on credit institutions.

This relates in particular to paragraph 133 of the Draft Guidelines pursuant to which Institutions should transmit to competent authorities the outcome of the suitability assessment for new members of the management body, paragraph 149 pursuant to which Institutions should inform competent authorities on a regular basis of any reassessments of collective suitability made, including their outcome and any measures taken as a result of the reassessment, and paragraphs 150 and 151 pursuant to which significant institutions should inform competent authorities of the assessment results regarding their heads of internal control functions and the CFO where these persons are not part of the management body.

Given this framework, it should be clarified that no communication and notification obligations are imposed by the Draft Guidelines where these obligations are not already set out in national legislative acts.

[16] In particular, recommendation 49 of the Spanish "Good Governance Code of Listed Companies" (CNMV, February 2015) states that "*[t]he nomination committee should consult with the company's chairman and chief executive, especially on matters relating to executive directors. When there are vacancies on the board, any director may approach the nomination committee to propose candidates that it might consider suitable.*"

[17] As it is the case of Spain and Portugal.

Q12: Are the guidelines with regard to the timing (ex-ante) of the competent authority's assessment process appropriate and sufficiently clear?

Title VII of the Draft Guidelines proposes that an *ex-ante* assessment by competent authorities is performed and that a suitability decision is taken by competent authorities prior to the appointment of any members of the management body and, for significant institutions, the heads of internal control functions and the CFO. In addition, paragraph 166 proposes detailed rules regarding the notification and assessment process; in particular, competent authorities should set out a maximum time period for their assessment of suitability which should not be less than three months (and not exceed four months).

Germany: These proposals again go well beyond the Current EBA Guidelines pursuant to which competent authorities may distinguish between the process applicable to members of the management body in its management function and in its supervisory function (see Chapter 10.2 of the Current EBA Guidelines) and no notification and assessment process by supervisory authorities is required for key function holders. They are also not covered by the mandates of the EBA and ESMA under Art. 91(12) CRD IV and Art. 9(1) MiFID II.

In light of the above, we kindly suggest that EBA and ESMA refrain from stipulating any *ex-ante* notification and assessment obligations currently not foreseen in the level 1 text and not go beyond the Current EBA Guidelines.

Italy, Spain and Portugal: The box in page 55 of the Draft Guidelines provides that the purpose of requiring an *ex-ante* filing is reducing "*the risk that members of the management body and key function holders* […] *might need to be replaced after the assessment by the competent authority*".

This risk can be neutralised if the corresponding corporate resolution includes a condition precedent preventing the appointment becoming effective until the competent authority has verified the suitability of the appointee.

This approach would avoid the risks of an *ex-post* negative assessment and at the same time avoid the main disadvantage of the *ex-ante* assessment (as stated in the Draft Guidelines, a higher length of the recruitment process). Consequently, this alternative could be expressly admitted in the final guidelines as a valid strategy available to Institutions, which would benefit from greater flexibility on recruitment processes.

In addition to considering such alternative as an equivalent to an *ex-ante* assessment, in relation to *ex-post* assessments, and in order to promote legal certainty, it would be useful for Institutions that the Draft Guidelines provide for a non-exhaustive list of examples of the "duly justified reasons" that would allow relying on an *ex-post* assessment. The guidelines could also envisage that the EBA and the ESMA feed such list from time to time with standard cases they have come across with in which an *ex-post* assessment was justified.

Italy: In relation to the previous comment, we would like to point out that the proposal for an *ex-ante* assessment of the suitability of members of the management body by the competent authority is a novelty in the Italian regulatory framework. So far such assessment has been conducted by the competent authorities *ex-post* (i.e. after the appointment of the relevant member of the management body) including a condition precedent in the relevant resolution, if needed.

Italian institutions falling within the scope of the Draft Consultation would have to adjust their procedures and relevant policies so as to make the recruitment process suitable for an *ex-ante* assessment by the competent authorities and this may require additional time and resources to implement the final guidelines.

Furthermore, the national corporate law may not allow for an *ex-ante* assessment. In fact, the shareholders may propose to the relevant shareholders' meeting the appointment of a member of the management body without the prior consent of the management body and/or of the nomination committee. We understand that this issue has already been considered in the

Consultation (i.e. Paragraph no. 127); therefore, we ask to clarify that, in this case or whenever the national applicable regulation may require so, an *ex-post* assessment should be conducted.

If an *ex-post* assessment is not deemed to be appropriate in case the shareholders submit a list of candidates to be appointed members of the management body, a separate approach could be adopted for executive positions. Specifically, an *ex-ante* assessment could be conducted for the persons to be appointed chairman of the management body and CEO, provided that the shareholders proposing the relevant candidate are able to submit to the relevant institution and, consequently, to the competent authority all the documents required. In this case, it should be noted that the *ex-ante* assessment could be useless if the proposed chairman and/or CEO were not appointed by the shareholders' meeting.

Finally, as pointed out in the Draft Guidelines, the *ex-ante* assessment will extend the time required for the recruitment process. This has a deep impact on the overall corporate governance of the relevant institution (for example, this may lengthen the interim period or vacancy of a member of the management body after the expiry of his or her term or after his or her resignation). This may also result in a breach of confidentiality in the recruitment process (meaning that the identity of the candidates for appointment may be revealed by the mass media), thus jeopardising the independence of the assessment process to be conducted by the management body of the institution.

Germany, Spain and Portugal: In addition, the establishment of a fixed minimum maximum duration for the competent authority's suitability assessment is not justified under any legal basis in the European Union. The proposed duration for the assessment of a single natural person's suitability is much too long compared to other mandatory durations of supervisory proceedings (such as, for example, the 60 working-day period for the assessment of acquisitions of qualifying holdings in institutions as set out in Art. 22 CRD IV and Art. 12 MiFID II).

Should nevertheless the proposed *ex-ante* assessment by competent authorities remain unchanged, the three/four-month maximums period should be either deleted or significantly shortened in order to give national legislators and competent authorities the required flexibility to set out appropriate rules or principles. However, if these comments are not be accepted, the Draft Guidelines should at least require competent authorities to allow Institutions, on a case-by-case basis, to transmit the application referred to the suitability assessment within a time frame shorter than the three/four-month period if necessary and appropriate by the specific circumstances (as provided, for examples, under Art. 31 of Commission Delegated Regulation (EU) No 241/2014 with reference to the application to carry out redemptions, reductions and repurchases of own funds instruments for the purposes of Art. 77 and 78 CRR).

Germany, Italy, Netherlands, Spain and Portugal: We suggest to add that the competent authorities should acknowledge that a speedy and timely decision may be necessary and welcome in certain circumstances, for example with important vacancies in the management body of listed institutions.

Q13: Which other costs or impediments and benefits would be caused by an *ex-ante* assessment by the competent authority?

Italy: See answer to Q12.

Q14: Which other costs or impediments and benefits would be caused by an *ex-post* assessment by the competent authority?

Italy: See answer to Q12.

Q15: Are the guidelines within Title VII regarding the suitability assessment by competent authorities appropriate and sufficiently clear?

Germany:

- Assessment by competent authorities of the suitability of the CFO and the heads of the internal control functions of significant institutions: With respect to the assessment by competent authorities of the CFO and the heads of the internal control functions of significant institutions please see our comments to Q12 above. In particular, the Draft Guidelines should be amended in order to leave the assessment of the suitability of any key function holders by competent authorities to national discretion.
- Assessment by competent authorities in the case of re-appointments: please see the paragraph "General Remarks" to the Draft Guidelines.

Netherlands, Spain and Portugal: We suggest to give appointees who have passed the assessment with respect to good repute, honesty and integrity a sort of "passport" to other member states. In other words: if an appointee passed this part of the suitability test in member state A, the appointee does not need to conduct a new test in member state B unless new facts arise which may lead to another outcome of the test. Is this option considered and is it possible despite the differences in national criminal and administrative law? Alternatively, in relation to section 27 of the Draft Guidelines (cooperation between competent authorities), the guidelines could provide that a simplified and quicker assessment (at least for requirements related to knowledge, skills and experience) could be carried out where another EU authority has assessed the suitability of a candidate within a certain period of time (e.g. within the last two years).

Q16: Is the template for a matrix to assess the collective competence of members of the management body appropriate and sufficiently clear?

Spain and Portugal: The template is not always clear on when it should be considered that a board member "adds value" for a particular requirement and many items included in the matrix are not related with knowledge or experience but with conduct matters, several of which are not "black or white" but gradable issues (e.g. setting tone at the top; social, ethical and professional standards; identifying the long-term interests of the company), so it is unclear how Institutions would have to complete the matrix.

Moreover, some of the items included in the matrix are embedded in the individual suitability assessment (e.g. social, ethical and professional standards) or in the general loyalty and responsibility duties of directors pursuant to corporate regulations (e.g. recognizing and raising the issue of conflicts of interest; identifying the long-term interests of the company; weighing the interests of all stakeholders; information-gathering) and thus all directors are expected to "add value" to these issues to be individually suitable, so it is not necessary to include them in the collective suitability matrix.

As regards the "collective score" on each item, some further guidance could be provided to help Institutions setting their scores.

Q17: Are the descriptions of skills appropriate and sufficiently clear?

Spain and Portugal: The description of skills should carefully consider if the director would be appointed as an executive or non-executive directors, since some of those skills are more or less necessary depending on the role of the director (e.g., negotiation and leadership skills are more relevant for executive directors than for non-executive directors). Thus, any and all directors do not need to meet all the same skills contemplated in the Draft Guidelines.

Q18: Are the documentation requirements for initial appointments appropriate and sufficiently clear?

Spain and Portugal:

- Paragraph 3.1: It should be clarified if the CV must include any professional background or if it has to be limited to a certain period of time (e.g. the last ten years) – as it has been traditionally required by certain competent authorities.
- Paragraph 6.1.g: The time estimate should be calculated in hours rather than days or at least clarify how many dedication hours are counted in a day.
- Paragraph 7.2: We understand that the requirement set forth in this paragraph whereby the institution should include a statement as to how the individual is to be situated in the overall suitability of the management body is not always necessary and could potentially instigate some discomfort between the various members of the board. Consequently, inclusion of this statement should be optional or only required where such a statement is relevant (e.g. where a new appointment is made to cover a specific and identified gap of the collective suitability of the board).

Netherlands: In practice we see that the forms to assess the repute, honesty and integrity of appointees are not very clear. Particularly in cases with a cross border context, filling out the different forms can be very time consuming. This should not be necessary. We suggest to introduce a new and standardised form in all member states, relevant for all types of financial undertakings regulated under EU law. This form could for example be used for authorisations, qualifying holdings, new appointments of members of the management body, and for the assessment of key function holders. Is this possible, despite the differences in criminal and administrative laws of the member states?

Q19: What level of resource (financial and other) would be required to implement and comply with the Guidelines (IT costs, training costs, staff costs, etc., differentiated between one off and ongoing costs)? If possible please specify the respective costs/resources separately for the assessment of suitability and related policies and procedures, the implementation of a diversity policy and the guidelines regarding induction and training. When answering this question, please also provide information about the size, internal organisation and the nature, scale and complexity of the activities of your institution, where relevant.

[No answer or comment.]

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